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Tax Legislation

North Carolina Lawmakers React to Recent Federal Tax Changes

North Carolina lawmakers are considering conforming with select federal tax law changes and decoupling from others.

The state Revenue Laws Study Committee has crafted draft legislation for potential consideration by the full Legislature when it reconvenes May 16. The proposal is a reaction to recent changes enacted through the 2017 federal tax act (Pub. L. No. 115-97) and the Bipartisan Budget Act of 2018.

North Carolina's corporate income tax law uses federal taxable income as the starting point in determining state taxable income, but links individual income tax liability to federal adjusted gross income. The state has its own deductions and exemptions and currently decouples from federal bonus depreciation and expensing rules.

Because of the way the state's tax code is structured, North Carolina's conforming to federal changes would have more of an impact on corporate than individual income tax liability, William W. Nelson, a partner with Smith, Anderson, Blount, Dorsett, Mitchell & Jernigan LLP in Raleigh, told Bloomberg Tax April 16.

Winners, Losers The draft bill generally conforms to the recent changes to federal tax provisions, according to Nelson. "This will be good news to some taxpayers such as small businesses who are exempt under the new law from certain onerous accounting method rules, but bad news for others," such as those impacted by a new net interest expense limitation, he said.

Among the federal tax provisions that North Carolina would decouple from under the draft legislation are those covering global intangible low-taxed income, qualified opportunity zones, repatriation, debt forgiveness for primary residences, and mortgage insurance premium and tuition deductions.

The proposed decoupling from federal foreign derived intangible income provisions "is unfortunate," Nelson told Bloomberg Tax. That is because conforming to that change would have made North Carolina more attractive to tech firms and pharmaceutical businesses selling into foreign markets, he said.

Important new compliance requirements and a provision to make permanent a temporary provision enacted by state lawmakers last year to prevent double sales taxation of certain inventory used in repair, maintenance, and installation services also are included in the draft bill, Nelson said.

State Revenue Boost According to a fiscal analysis of the draft legislation, the changes being eyed would boost state revenue by about $312 million over four years.

Among the more significant fiscal impacts from conforming with federal changes are state revenue gains stemming from business income tax deductions. Following those revisions was estimated to result in revenue gains of $80 million during the fiscal year that begins in July and $63 million during the next year.

Conforming to changes in the federal tax provisions that simplify small business accounting methods were estimated to result in revenue losses to North Carolina of $35 million during the upcoming fiscal year and $31 million during the next.

A detailed look at the draft legislation was posted by Nelson April 16 on his law firm's website.

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☐ *The draft legislation pending in North Carolina is at http://src.bna.com/xYj.*

The accompanying fiscal analysis is at http://src.bna.com/xZu.

A February 2017 NCDOR memo on the impact of federal changes is at http://src.bna.com/xZM.

Smith, Anderson, Blount, Dorsett, Mitchell & Jernigan, LLP's analysis is at http://www.smithlaw.com/resources-publications-1109.

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